

Revision of Rating Methodology for "Rating Perspectives for Subsidiary Companies"

Japan Credit Rating Agency, Ltd. (JCR) hereby announces that it has revised its rating methodology "Rating Perspectives for Subsidiary Companies" to "Rating Methodology for Group Companies of Corporate Group." JCR revised the Rating Methodology as a result of considerations that were announced in its press release "JCR Solicits Public Comments on Rating Methodology for Group Companies of Corporate Group" dated July 13, 2022, and JCR decided the Rating Methodology as proposed at the time of requesting the public comments on it.

JCR revised the "Rating Methodology for Financial Groups' Holding Companies and Group Companies" in accordance with the above revision. The main changes are the modifications to the descriptions regarding the credit rating of group companies of financial groups.

The revised rating methodologies will be posted on the "Rating Methodologies: Corporates" page (https://www.jcr.co.jp/en/rrinfo/meth_corp/) and "Rating Methodologies: Financial Institutions" page (https://www.jcr.co.jp/en/rrinfo/meth_finance/) of JCR's website.

In accordance with the revisions, JCR will review the long-term issuer ratings of about 20 companies within this fiscal year, about 70% of which are group companies of financial groups and the rest are group companies of industrial corporation groups. The review may result in a one-notch increase in the rating.

In the request for the public comments, there was an opinion that a careful explanation should be provided from theoretical and case-study perspectives when revising rating methodologies and when making changes to individual issuers' ratings, etc. based on such revisions. With regard to this point, JCR will make an effort to provide specific and careful explanations in press releases, comments, etc.

Shigenobu Tonomura, Kengo Sakaguchi

Japan Credit Rating Agency, Ltd.

Jiji Press Building, 5-15-8 Ginza, Chuo-ku, Tokyo 104-0061, Japan
Tel. +81 3 3544 7013, Fax. +81 3 3544 7026

Information herein has been obtained by JCR from the issuers and other sources believed to be accurate and reliable. However, because of the possibility of human or mechanical error as well as other factors, JCR makes no representation or warranty, express or implied, as to accuracy, results, adequacy, timeliness, completeness or merchantability, or fitness for any particular purpose, with respect to any such information, and is not responsible for any errors or omissions, or for results obtained from the use of such information. Under no circumstances will JCR be liable for any special, indirect, incidental or consequential damages of any kind caused by the use of any such information, including but not limited to, lost opportunity or lost money, whether in contract, tort, strict liability or otherwise, and whether such damages are foreseeable or unforeseeable. JCR's ratings and credit assessments are statements of JCR's current and comprehensive opinion regarding redemption possibility, etc. of financial obligations assumed by the issuers or financial products, and not statements of opinion regarding any risk other than credit risk, such as market liquidity risk or price fluctuation risk. JCR's ratings and credit assessments are statements of opinion, and not statements of fact as to credit risk decisions or recommendations regarding decisions to purchase, sell or hold any securities such as individual bonds or commercial paper. The ratings and credit assessments may be changed, suspended or withdrawn as a result of changes in or unavailability of information as well as other factors. JCR receives a rating fee paid by issuers for conducting rating services in principle. JCR retains all rights pertaining to this document, including JCR's rating data. Any reproduction, adaptation, alteration, etc. of this document, including such rating data, is prohibited, whether or not wholly or partly, without prior consent of JCR.

JCR is registered as a "Nationally Recognized Statistical Rating Organization" with the U.S. Securities and Exchange Commission with respect to the following four classes. (1) Financial institutions, brokers and dealers, (2) Insurance Companies, (3) Corporate Issuers, (4) Issuers of government securities, municipal securities and foreign government securities.

JCR publishes its press releases regarding the rating actions both in Japanese and in English on the same day. In case that it takes time to translate rating rationale, JCR may publicize the summary version, which will be replaced by the full translated version within three business days. (Regarding Structured Finance products, JCR only publicize the summary version in English.)

Rating Methodology for Group Companies of Corporate Group

1. Scope of this Methodology and its Relations with Other Methodologies

This rating methodology is applied to group companies of domestic groups with business corporations as core companies and such groups with financial corporations as core companies. However, for financial institutions and the like under the prudential regulation, the "Rating Methodology for Financial Groups' Holding Companies and Group Companies" shall be applied preferentially. Regarding group companies with the overseas business corporations and financial corporations as the core companies, this rating methodology shall be applied mutatis mutandis after making necessary adjustments based on the legal and accounting systems of the location of those companies.

2. Long-term Issuer Rating of Group Companies

(1) Main Components of Rating Methodology

There are two methods for assigning a long-term issuer rating to a group company of a corporate group: top-down approach, which uses the corporate group's creditworthiness as a starting point and takes into account the degree of likelihood of future group support; and bottom-up approach, which uses the group company's stand-alone creditworthiness assessment as a starting point and adds the degree of likelihood of group support to this. In principle, JCR adopts the top-down approach for rating of group companies. The term "group companies" as used in this rating methodology refers to subsidiaries, affiliates, and other companies, which JCR considers belong to a specific corporate group from various perspectives, such as capital, personnel, and business relationships.

JCR mainly takes into account the following factors to determine a long-term issuer rating for the group company of the corporate group.

- Likelihood of support by the corporate group for the group company
 - Degree of Control and Involvement of Corporate Group in Group Company
 - Degree of Managerial Importance in Corporate Group
- Stand-alone Creditworthiness of Group Company (Stand-alone Assessment)
- Creditworthiness of Corporate Group

(2) Support by the corporate group to the group company

Support by the corporate group to the group company is judged comprehensively based on an evaluations from two axes: degree of control and involvement evaluation and degree of managerial importance evaluation. The key point of the top-down approach is recognition of a probability that the corporate group will provide remedial support, based on reasonable grounds, when the creditworthiness of the group company declines. In addition, it is usually assumed that the corporate group will often provide strategic support such as additional investments and loans to the group company, or further enhancement of ties between the corporate group and the group company, for the realization of the group strategy and sustainable growth. JCR will judge support of the corporate group from the perspectives of both remedial and strategic supports.

(i) Degree of Control and Involvement of Corporate Group in Group Company

The evaluation of control and involvement is based on (i) ratio of voting rights held by the corporate group in the group company, (ii) degree of involvement of the corporate group in the decision-making process of the group company, (iii) status of dispatch of directors and others, and (iv) status of establishment and utilization of group CMS and credit lines or integrity of management control. The higher the ratio of voting rights, the greater the degree of control and involvement of the corporate group, but if the ratio is not 100%, JCR considers the effective controlling power of the corporate group, taking into account the composition of other shareholders.

With regard to listed subsidiaries, they are positioned as leading companies in the corporate group, and their sharing of strategies and business ties are relatively strong. On the other hand, the perspective of ensuring independence is becoming increasingly important amid the increasing demand for more sophisticated group governance, and the degree of control and involvement by a company is highly constrained. Furthermore, for companies that are fifty-fifty joint ventures, the positioning and importance in the two corporate groups in terms of business strategy are not consistent. For these companies, JCR will make a comprehensive judgment of the degree of control and involvement by carefully examining how the group company joined the group or how it was established, current status of governance, and changes in positioning in the two groups.

(ii) Degree of Managerial Importance in the Corporate Group

The degree of managerial importance is evaluated from the perspectives of (i) degree of strategic importance (whether the business segment to which the group company belongs is important for the corporate group's long-term vision and medium-term management plan) and (ii) degree of functional importance (whether the group company performs important functions in forming the value chain and group infrastructure for business operations). The more important a group company is in the corporate group, the closer the creditworthiness of the group company becomes to that of the corporate group.

(3) Stand-alone Creditworthiness of Group Company (Stand-alone Assessment)

The stand-alone creditworthiness of a group company refers to the creditworthiness of the group company on its own, based on the evaluation of its business and financial bases that have been formed through its relationship with the corporate group (formed by the core company). JCR does not assume a fully independent company with no consideration of ties to the group in terms of people, goods, money, and business. The target of long-term issuer rating is unambiguously the group company. Assuming that the group creditworthiness declines and support cannot be obtained from the parent company and others, or that the group company leaves the corporate group, JCR will evaluate the creditworthiness of the group company alone.

(4) Creditworthiness of Corporate Group

With regard to the creditworthiness of a group company, JCR will evaluate the creditworthiness of the corporate group to which the group company belongs in order to determine the base point for notching down when the top-down approach is applied. With regard to the creditworthiness of a corporate group, JCR basically analyzes the consolidated business and

financial bases of the corporate group, but adjustments may be made to the consolidated data in accordance with the actual condition of the group. The creditworthiness of a corporate group can be regarded as the underlying strength that supports its group companies. No matter how strong the degree of control and involvement or managerial importance, if the creditworthiness of the corporate group is low, it will have a negative impact on the degree of likelihood of group support.

(5) Consideration of Approach to be Applied

Through (2) through (4) above, JCR evaluates the likelihood of support by the corporate group to the group company to determine whether the top-down approach can be applied. If possible, JCR determines the rating of the group company by applying notching (difference in creditworthiness between the group and the group company) according to the likelihood of support.

However, during the evaluation process, it may be determined that the top-down approach should not be applied even if a company falls under the category of group companies. For example, the top-down approach may not be applied in cases where the core company is an investment fund and the like, and the group company is a net investment target, and it is therefore easily assumed that the group company will be replaced in the future, even if the ratio of voting rights is sufficiently high.

If it is recognized that the degree of likelihood of remedial or strategic support by the corporate group will change in the future due to a change in management policy or strategy of the corporate group or a change in the investment ratio, JCR will flexibly review whether the top-down approach should be applied.

If the stand-alone assessment exceeds the top-down approach assessment, JCR gives priority to the stand-alone assessment for the rating of the group company. Even in such cases, in principle, the rating level of the group company shall not exceed the group creditworthiness. However, if the influence of the corporate group is judged to be limited due to the fact that the group company is listed on a stock exchange or other factors, the creditworthiness of the group company may exceed that of the corporate group to a certain degree.

For companies that do not fall under the category of group companies or whose importance to the corporate group is not considered at a high degree, stand-alone assessment is the general rule. However, even for such companies, the creditworthiness of the corporate group may be reflected if the likelihood of remedial or strategic support by the corporate group is recognized to more than a certain degree.

Because of the possibility of human or mechanical error as well as other factors in the information herein, JCR makes no representation or warranty, express or implied, as to accuracy, results, adequacy, timeliness, completeness or merchantability, or fitness for any particular purpose, with respect to any such information, and is not responsible for any errors or omissions, or for results obtained from the use of such information. Under no circumstances will JCR be liable for any special, indirect, incidental or consequential damages of any kind caused by the use of any such information, including but not limited to, lost opportunity or lost money, whether in contract, tort, strict liability or otherwise, and whether such damages are foreseeable or unforeseeable. Information herein is statements of opinion, and not statements of fact as to credit risk decisions or recommendations regarding decisions to purchase, sell or hold any securities such as individual bonds or commercial paper. JCR retains all rights pertaining to this document. Any reproduction, adaptation, alteration, etc. of this document, is prohibited, whether or not wholly or partly, without prior consent of JCR.

Japan Credit Rating Agency, Ltd.

Jiji Press Building, 5-15-8 Ginza,
Chuo-ku, Tokyo 104-0061, Japan
Tel. +81 3 3544 7013, Fax. +81 3 3544 7026

Rating Methodology for Financial Groups' Holding Companies and Group Companies

1. Scope of this Methodology and its Relations with Other Methodologies

This rating methodology covers financial groups' holding companies and group companies, which have financial institutions (including deposit-taking financial institutions, insurance companies, securities companies, etc.) that are subject to prudential regulation, as core companies.

As for rating methodologies for holding companies and group companies, JCR has published "Rating Methodology for a Holding Company" and "Rating Methodology for Group Companies of Corporate Group" which are general rules that can apply to all corporate ratings. Based on views shown in these rating methodologies as general rules, JCR added adjustments for characteristics of financial institutions which are under prudential regulation to this rating methodology. In cases of considering issues that are not mentioned in this rating methodology, therefore, JCR refers to general rules that can apply to all corporate ratings.

This rating methodology does not cover holding companies and group companies of financial groups, which have nonbanks and the like that are not subject to prudential regulation, as core companies. In cases where it is considered that some regulations, supervisions or any other reasons restrict probabilities of support from financial groups to the holding companies and group companies by the authorities, this methodology shall apply *mutatis mutandis* to such companies.

2. Long-term Issuer Rating for Holding Companies

(1) Major Factors to be Considered

Based on evaluations on overall financial groups' creditworthiness (group creditworthiness) as the starting point, JCR mainly takes into account the following factors to determine long-term issuer rating for holding companies of financial groups.

- Holding Companies' Controlling Power over Group Companies
- Holding Companies' Cash Flow Balance and Financial Structure
- Resolution Regime that is Applied to Holding Companies

(2) Controlling Power Over Group Companies

Holding companies in many cases rely on cash they receive such as commissions and dividends from their subsidiaries for funds for repayment of external financial obligations. For this reason, it is an important point whether they can have a full controlling power over subsidiaries (group controlling power) in evaluation of their abilities to repay debt. JCR determines their group controlling power by factors including the following: (i) purpose of establishment; (ii) investment ratio held by holding companies and their involvement in management of subsidiaries including personnel relationships; and (iii) strength of power and authority over subsidiaries. If their group controlling power is not considered sufficient, rating level of holding companies may be far below the group creditworthiness.

(3) Cash Flow Balance and Financial Structure

As holding companies in many cases rely on cash they receive such as commissions and dividends from their subsidiaries for funds for repayment of external financial obligations, JCR thinks that putting emphasis on cash flow analysis, which is applied to evaluating industrial corporations, is necessary for evaluating holding companies of financial groups. Also, there are risks in cases of financial groups that use of cash from subsidiaries might be restricted in some cases, although holding companies' group controlling power is strong. This is because there are cases in which dividend payment from core subsidiaries to holding companies may be restricted due to prudential regulation in some cases.

In light of the above situations, JCR determines whether holding companies can keep cash flows required for debt repayment on an ongoing basis, if use of cash from subsidiaries is restricted, through evaluation of balance between cash inflow and cash outflow (cash flow balance). Specifically, JCR confirms several factors such as (i) ratio of stable revenues other than dividends to cash inflow and dividend stability and (ii) sufficiency of cash inflow in comparison with cash outflow (cash inflow and outflow include those related to principal redemption on assets and liabilities. In evaluation of these factors, JCR uses double leverage ratio, which is calculated by dividing stocks of subsidiaries and affiliates by equity capital of holding companies on an unconsolidated basis as a reference indicator. Double leverage is a structure where a holding company acquires stocks of subsidiaries and affiliates through external debt and those subsidiaries further externally raise funds. In cases where the double leverage ratio is high due to the external debt used for acquisition of stocks of subsidiaries and affiliates, it is becoming increasingly likely that fixed cash outflow for debt repayment and others will not be covered by stable cash inflow.

A holding company, which has problems with cash flow balance, is susceptible to restrictions on use of cash from subsidiaries when there are such restrictions. In such cases, JCR considers notching down the rating from the group creditworthiness, even if it has a strong group controlling power.

In evaluation of cash flow balance using double leverage ratio as a reference indicator, JCR conducts the evaluation based on not only conditions at the current time, but future perspectives. Future financial management policies as well as track record in the management are to be taken into consideration.

In recent years, investments by holding companies have diversified thanks to developments such as deregulation of investments by a bank holding company in financial related IT firms. JCR also checks whether investments by holding companies in entities other than core group companies can increase its financial risk.

(4) Resolution Regime to be Applied

JCR takes into account the fact that treatment by the authorities upon resolution might be different between the holding company and group companies under its umbrella in the case of financial groups. This is because in cases where resolution regimes that are defined under the Deposit Insurance Act and others are applied to a financial group, it is assumed that remedial measures for creditors of subsidiary companies such as banks will be taken by the government, but such measures will not be taken for the holding company.

JCR sees that the risk of occurrence of such cases is relatively large for financial groups, to which SPE Resolution, a method by which loss burden at the time of a resolution is to be intensively borne by shareholders and creditors of a

holding company, shall be applied in principle by laws and ordinances or as policies by the government. The authorities in Japan, FSA, showed its policy to adopt SPE Resolution at the time of a resolution to financial groups called Covered SIBs, which are designated as SIBs, to which TLAC regulations are applied. In cases where Specified Measures Under Item (ii) defined under the Deposit Insurance Act are taken, the financial group's loss shall be intensively absorbed by shareholders and creditors of the holding company, if the resolution measure is taken in accordance with FSA's policy.

A situation where while remedial measures that benefit creditors of subsidiaries such as banks are taken by the government, such measures are not taken for holding companies can happen to financial groups, for which adoption of SPE Resolution is shown in advance. The remedial measures by the government are taken basically for the purposes of maintaining financial order in the countries and the regions and stabilization of the financial system. From the perspectives of achieving these objectives, it is likely that authorities may consider that protection of creditors of holding companies is less important than that of creditors of subsidiaries such as banks. There was a case in Japan where a holding company was liquidated while creditors of a bank in the financial group were protected in resolution process, for which Measures Under Item (iii) defined under the Deposit Insurance Act were taken.

(5) Long-term Issuer Rating for Holding Companies Having Sufficient Strong Group Controlling Power

(i) Views

In determination of long-term issuer rating for holding companies which have sufficiently strong group controlling power, JCR judges necessity of notching down and the degree of it in a comprehensive manner, taking into account risks related to cash flow balance and those related to resolution regime together. Concerning risks related to resolution regime, JCR reflects such risks according to a probability of actual occurrence of a situation where loss burden is intensively borne by creditors of the holding company. For holding companies, for which application of SPE Resolution is indicated in advance in the authorities' policy, JCR sees that it is much more likely that the creditors of the holding company will intensively bear the group's loss burden than in the case of holding companies, for which such application is not indicated in advance. Meanwhile, such probability will decline, if preventive measures are taken including capital injection by the government to a sound bank or group prior to a stage where the group is identified as being at the point of non-viability (PON), which requires resolution measures. JCR therefore takes into account the degree of a probability that preventive measures can be taken for sound banks and groups that are not authorized as being at PON.

(ii) Holding Companies, for Which Application of SPE Resolution is Indicated in Advance

JCR notches down long-term issuer rating for holding companies from their group creditworthiness in countries and regions, for which application of SPE Resolution is indicated in advance, and which JCR judges are facing large restrictions on preventive measures for sound banks and groups that are not authorized as being at PON, seeing it is likely that risks related to resolution regime can relatively easily come to the surface in such cases. The level of notch down is in principle 1 in cases where it is determined that there are no problems in group creditworthiness. There might be many cases for holding companies in the U.S. and Europe where JCR judges in this way. In cases where JCR notches down the rating due to reasons related to resolution regime when it is

determined that there are no problems in group creditworthiness, JCR does not additionally notch down even if there are problems with cash flow balance. In cases where there are no problems in group creditworthiness, JCR sees that risk inherent in the holding company can be fully reflected by 1 notch down.

For holding companies in countries and regions, for which application of SPE Resolution is indicated in advance, but which JCR judges are facing less restrictions on preventive measures, necessity to reflect risks related to resolution regime is relatively small. For this reason, JCR basically places emphasis on risks related to cash flow balance for considering the long-term issuer rating. JCR reflects risks related to resolution regime when group creditworthiness is relatively low. Specifically, in cases where the group creditworthiness is relatively high at equivalent to A or higher than A, JCR assigns the same rating as the group creditworthiness to the holding company, when JCR judges that there are no problems with cash flow balance. When JCR judges that there are problems with cash flow balance, JCR notches down the rating by 1 notch. In cases where the group creditworthiness is equivalent to A- or lower than A- and application of SPE Resolution is indicated in advance, JCR reflects risks related to resolution regime in ratings for the holding companies irrespective of cash flow balance, and notches down the rating in principle by 1 notch. There might be many cases for holding companies in Japan where JCR judges in this way. JCR sees that the possibility of application of preventive measures for sound banks and groups such as Measures Under Item (i) or Specified Measures Under Item (i) defined under the Deposit Insurance Act at the time of financial crisis for Japanese financial groups is considerably high. Views on restrictive factors for the preventive measures, however, may change depending on the authorities' attitudes, political, financial, and economic environment.

(iii) Holding Companies, for Which Application of SPE Resolution is Not Indicated in Advance

For holding companies, for which application of SPE Resolution is not indicated in advance, JCR notches down the rating in principle by 1 notch when there are problems with cash flow balance, basically placing emphasis on the cash flow balance in determination of rating. Concerning risks related to resolution regime, JCR incorporates a probability of actual occurrence of a situation where loss burden is intensively borne by creditors of the holding company into the ratings, judging it in a comprehensive manner based on political situations, the authorities' policies and attitudes, etc. on a case-by-case basis.

(iv) Intermediary Holding Companies

For intermediary holding companies, if it is recognized that it is highly likely that support from the group through the parent company will be extended, JCR sometimes gives the same rating as the group creditworthiness to them, even if there are problems with cash flow balance.

(v) Factors for Expansion or Reduction of Notching

JCR considers expanding notching in all cases as the group creditworthiness lowers and the possibility of being placed under resolution regime increases. In these cases, JCR gives a rating in line with definitions of rating symbols based on distance to loss. As a result, notching might be larger than 1 notch. There are cases where mutual

support in the group is strictly restricted, depending on countries and regions. In these cases, JCR notches down by more than 2 notches.

3. Long-term Issuer Rating for Group Companies

(1) Major Factors to be Considered

JCR determines the long-term issuer rating for financial groups' group companies other than holding companies, taking into account both the sole creditworthiness derived from evaluations of those group companies' sole earnings and financial structure and likelihood of future financial support by the group (group support) together. There are two methods to reflect likelihood of group support in the rating: (i) top-down approach, under which JCR incorporates group support into the ratings based on evaluation of group creditworthiness and (ii) bottom-up approach, under which JCR incorporates group support into the ratings based on evaluation of group companies' sole creditworthiness. JCR determines the long-term issuer rating for group companies, primarily taking into consideration the following factors under these two methods.

- Group Companies' Importance
- Group Companies' Sole Creditworthiness
- Group Creditworthiness
- Group Companies' Size

(2) Group Companies' Importance

JCR places the group companies' importance in their groups as the most important factor in evaluation of likelihood of group support. As explained as general rules that can be applied to all corporate ratings in common in "Rating Methodology for Group Companies of Corporate Group," JCR determines its evaluations by examining the degree of control and involvement in the group companies by the group and their strategic and functional positioning in group management.

(3) Group Companies' Sole Creditworthiness

JCR considers it is necessary to reflect sole creditworthiness of group companies in their ratings, depending on situations, even in the case of top-down approach. This is because it is necessary to consider restrictions under prudential regulation for core companies and holding companies. Unlike industrial corporation groups, core companies and holding companies in financial groups are subject to prudential regulation including capital adequacy ratio regulation or prompt corrective action. Thus, they cannot support group companies in an unlimited way where it exceeds a certain level required for soundness under the regulation.

(4) Group Creditworthiness

JCR takes into account group creditworthiness as not only a starting point for notching down under the top-down approach, but a factor for determination of the degree of it. This is because it is considered it will become more likely that risks related to restrictions under prudential regulation described above will come to the surface in cases where group creditworthiness is low, because core companies' or holding companies' financial margins have been lowered in such

cases. Deterioration of group creditworthiness can work against likelihood of group support, and becomes a factor for expansion of difference between group creditworthiness and group companies' ratings.

(5) Group Companies' Size

In general, large group companies' contributions to the group in terms of business base and earnings are large, and their importance in the group can be considered high in many cases. Large size of group companies will increase likelihood of group support and work for their creditworthiness. This is also true for financial groups' group companies.

However, there are cases where JCR negatively reflects large size of financial groups' group companies measured by total assets in their ratings unlike group companies of industrial corporation groups. This is because financial groups are subject to prudential regulation and possibility of their violations of this regulation increases when size of their group companies becomes large as compared with the groups' financial strength. Restrictions under prudential regulation can more come to the surface as the group creditworthiness lowers. As group creditworthiness lowers, difference between group creditworthiness and group companies' ratings expands, because large size of group companies can weaken likelihood of group support.

(6) Top-down Approach and Bottom-up Approach

For group companies which belong to financial groups and are recognized as highly important for the groups, JCR takes top-down approach. In this case, while JCR assigns the same long-term issuer rating as group creditworthiness to the core group companies, which assume major parts of their groups' business bases and earnings. JCR notches down the ratings for group companies other than core companies from group creditworthiness. Notching between the group companies and group creditworthiness under top-down approach is usually 0 to 3. The most important factor for determination of this notching is importance for the group described in (1). For financial groups, however, notching from group creditworthiness sometimes expands as a result of additional evaluations on group companies' sole creditworthiness, group creditworthiness, and group companies' size as described in (3), (4), and (5).

JCR makes much account of substantial aspects in determination of importance in the financial groups. In cases of group companies under financial groups, it is not unusual that investment ratios by core companies or holding companies for some group companies are restricted, even though they are important for the groups, due to restrictions under laws and regulations or in consideration of impact on financial indicators. In these cases, JCR sometimes treats these group companies as equivalent to group companies with high investment ratios, in consideration of intensity of ties in terms of organization and business operations.

For group companies which are not considered much important for the financial groups, JCR considers taking bottom-up approach, if likelihood of group support is recognized to more than a certain degree. The degree of the notching up from the group companies' sole creditworthiness is 1 or 2 in many cases.

Upper limit of the group companies' ratings is, in principle, group creditworthiness, even if their sole creditworthiness is considered higher than group creditworthiness, based on the fact that the groups can basically freely use group companies' capital and other resources. In cases where it is considered that keeping the group companies' creditworthiness at a certain level even at the cost of the groups' financials, etc. is very important for the groups, JCR considers giving

higher ratings that exceed the group creditworthiness to such group companies. For example, banks specializing in asset administration services which undertake and administer important assets of customers of core companies in the groups are such cases.

(7) Management Integration Among Companies in the Same Business Category

(i) Evaluation Method

In the face of tough earnings environment due to decline of population and prolonged low interest environment, movements to keep financial functions or soundness through management integration among companies in the same business category are continuing in Japan's financial industry. These movements include joint establishment of a holding company by several banks and then formation of a new financial group under the holding company or some banks' joining other financial banking groups. Through these movements, there are an increasing number of cases where there are group companies belonging to the same industry as the core company or where there are several core companies belonging to the same industry in the same financial groups.

For group companies which joined groups for the purpose of management integration, JCR takes top-down approach and assigns a rating close to group creditworthiness to them. This is based on the following: (i) Japan's financial environment makes importance of management integration and subsequent integrated management of groups higher; (ii) there are many cases where integration of groups are pursued in the field of important practical operations such as systems; (iii) financial groups have strong incentives to prevent overall groups' confidence and reputation from being impaired through their treatments for group companies.

(ii) Views on Group Companies' Importance in Management Integration

Japan's financial industry is facing stagnant needs for financing and intensified competition in the declining population and structural fund surplus situations, shrinking interest margin due to prolonged low interest rate environment, increasing threats from new entrants from different industries such as IT and retail companies, and so on. Management integration is considered effective for realization of goals for these challenges including expansion of sales channels and regions, increase of added-value of products and services, business diversification, higher efficiency including reduction of expenses. Based on this position of management integration, JCR sees that JCR can judge that importance of management integration and groups' integrated operations is high in many cases.

JCR sees that groups' integration in important practical operations including integration of systems, unification of administrative rules, sharing of administrative functions, unification of personnel system, personnel exchange in many fields, is indicating high importance of management integration and group companies. JCR also considers that disorders that can be expected when the groups do not extend necessary support to the group companies which are integrated to the group in terms of practical operations should be taken into account in judging their importance.

In cases where group companies belonging to the same industry, weakening or breakdown of financial bases may have a negative impact on financial order in countries and regions and stability of the financial system. It is essential for financial groups to keep confidence and good reputation from the market, customers, regional societies, the authorities, etc. in conducting their businesses. Failures in taking appropriate measures for group companies

and then causing negative impact on financial order, etc. may significantly damage the groups' confidence and reputation and may also shake the groups' business itself. For this reason, it is very important to keep financials of subsidiaries in sound status.

(iii) Overall Evaluation

JCR assigns the same long-term issuer rating as group creditworthiness to group companies belonging to the same industry which joined the group for the purpose of management integration and are highly important for the group, as they satisfy the assumptions described in (7) (ii) above.

In cases where the degree of satisfaction for the assumptions described in (7) (ii) is recognized as weak and the importance of group companies is not considered very high, JCR notches down the rating for group companies by 1 notch or more from group creditworthiness. For example, if integration of systems is considered insufficient, policies are undetermined, or feasibility is unknown, JCR considers notching down by around 1 notch from group creditworthiness, till JCR can confirm strong integration. In cases where JCR judges that management integration is not strategically very important and the integration is strongly considered as relief, JCR considers notching by 2 notches or more under the top-down approach in line with evaluation of the importance, or applying the bottom-up approach to the ratings.

Even in cases where JCR judges that importance of group companies is very high, JCR sometimes does not assign the same ratings as group creditworthiness to such group companies, as a result of evaluations on group companies' sole creditworthiness, group creditworthiness, and group companies' size as described in (3), (4), and (5). That is to say, in cases where there is a difference of more than 2 notches between group companies' sole creditworthiness and group creditworthiness, JCR considers notching down by 1 notch or more for the group companies from group creditworthiness, excluding when the group companies are small. In particular, if there is difference between the group companies' sole creditworthiness and group creditworthiness and the group creditworthiness cannot be said as high being equivalent to A- or lower than A-, JCR considers notching down by 2 notches or more.

There are cases where sole creditworthiness of core companies which assume financial burden required for groups' support for group companies is higher than group creditworthiness. In such cases, JCR considers setting the sole creditworthiness of the core companies as the starting point for the notching.

Because of the possibility of human or mechanical error as well as other factors in the information herein, JCR makes no representation or warranty, express or implied, as to accuracy, results, adequacy, timeliness, completeness or merchantability, or fitness for any particular purpose, with respect to any such information, and is not responsible for any errors or omissions, or for results obtained from the use of such information. Under no circumstances will JCR be liable for any special, indirect, incidental or consequential damages of any kind caused by the use of any such information, including but not limited to, lost opportunity or lost money, whether in contract, tort, strict liability or otherwise, and whether such damages are foreseeable or unforeseeable. Information herein is statements of opinion, and not statements of fact as to credit risk decisions or recommendations regarding decisions to purchase, sell or hold any securities such as individual bonds or commercial paper. JCR retains all rights pertaining to this document. Any reproduction, adaptation, alteration, etc. of this document, is prohibited, whether or not wholly or partly, without prior consent of JCR.

Japan Credit Rating Agency, Ltd.

Jiji Press Building, 5-15-8 Ginza,
Chuo-ku, Tokyo 104-0061, Japan
Tel. +81 3 3544 7013, Fax. +81 3 3544 7026